



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

EXEMPT AND
NON-PROFIT ENTITIES
DIVISION

Date:

OCT 29 2001

Contact Person: [REDACTED]

Identification Number: [REDACTED]

Contact Number: [REDACTED]

Fax: [REDACTED]

Employer Identification Number: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were incorporated on [REDACTED]. Your Articles of Incorporation state, in part, that your purposes include the following:

- (a) To promote the general welfare of the residents of the [REDACTED] through the creation and operation, in a manner consistent with its general and public welfare purposes, of a year-round public market at the City-owned [REDACTED], located at [REDACTED] and to encourage patronage and business at the [REDACTED] for the benefit of the citizens of [REDACTED] and surrounding areas.
- (b) To plan, finance, construct, maintain, operate and manage the [REDACTED] in so doing, to promote the related public purposes.
- (c) In furtherance of and subject to the purposes and objects set forth above, the Corporation shall also have the power to engage in any lawful act or activity for which nonprofit corporation may be formed under [REDACTED]

On [REDACTED], you entered into an agreement with the City concerning the [REDACTED] Project ([REDACTED] Project). Pertinent provisions of the agreement include the following:

WHEREAS, the City wants to enter into a Management Agreement with an independent non-profit entity to manage the [REDACTED] [REDACTED], the [REDACTED] the [REDACTED] and any common or empty areas within the former

_____ and all publicly-owned parking adjacent thereto; i.e., the _____ Project; and

WHEREAS, it is the intention of the City to appropriate monies for the _____ Project sufficient to meet its management and operation needs until such time as it becomes self-supporting, provided, that future availability of funding and its appropriation is subject to the standard procedures of the City's yearly budget allocation process, and provided that _____ shall have no responsibility or liability to provide financial support for the _____ Project over or beyond the City budget allocation and revenue generated by the _____ Project; and

WHEREAS, THE City and _____ desire to arrange for the orderly lease, management, operation and Marketing of the _____ Project, to include the _____ the _____ the _____ and any vacant space within the _____ Project from time to time.

PURPOSE. The City of _____ desires to create a year-round public retail establishment at the former Civic Auditorium, located at _____ and _____ in _____. The site is adjacent to the existing _____. _____, a non-profit corporation has indicated its desire to be the entity which as an agent for the City of _____ will develop and manage the _____ Project in a manner consistent with its general and public welfare purposes to bring the patronage and business for the benefit of the citizens of _____ and surrounding areas; to plan, construct, maintain, operate and manage the _____ Project, with related functions and activities; and to serve a public purpose.

APPOINTMENT AND ACCEPTANCE OF _____ City hereby appoints _____ as the City's agent for the purposes of supervising, leasing, managing, marketing, maintaining, operating and developing the _____ Project upon the terms and conditions set forth below. _____ shall have, as its Initial Board Members, eight (8) persons selected by the Mayor, and three (3) persons selected by the City Council all of whom shall be confirmed by City Council, and up to two (2) other persons as deemed necessary by the other Board members. Elected officials of the State of _____ and City of _____, and employees of the City of _____ (herein, collectively, "Public Representatives") may be members of the Board provided, however, Public Representatives shall not be voting members of the Board and, provided further, the Board shall have at least three (3) non-Public Representatives. After the initial appointment, all Board members shall be added by a majority vote of the existing Board members, _____ accepts the appointment and agrees to furnish the services of its organization for the management of the _____. Notwithstanding this Section, the City retains the ultimate control and use of the Premises.

TERM. This agreement shall be for a term of three (3) years commencing on _____ ("Effective Date") and terminating on _____ ("Initial Term"). The parties intend that the rights, power, authority, responsibilities and obligations of _____ as provided in this Agreement shall become effective during the initial term over three phases, each expiring at the end of the Initial Term but commencing on the dates set

forth below:

POWER AND AUTHORITY. [REDACTED] shall have the power and authority to do the following:

- Develop and sustain an advertising and promotion program for the entire marketplace premises.
- Develop and implement operating procedures for the [REDACTED] Project including staffing, administrative resources, policies and procedures which address the requirements of all applicable regulatory entities; and
- Commencing with the Second Phase, [REDACTED] will hire a full-time Manager, the expense of whose employment is an operating expense of the Market to manage and operate the [REDACTED] Project on a day-to-day basis, including leasing, advertising and marketing the vendor stalls to retailers and the performance of all other duties normally associated with the maintenance and operation of a facility of this type; and
- Investigate all references of prospective tenants and service providers to the [REDACTED] Project; and
- Prepare, negotiate, sign, deliver, renew, amend, perform and cancel agreements all on behalf of the City, for the leasing of space to vendors and all other tenants, and other documents and instruments in connection with such leases. The forms for all such leases, documents and instruments shall be approved in writing by the City prior to use by [REDACTED]. Any modifications, changes or deletions to such leases, documents or instruments shall be approved in writing by the City prior to the implementation of such modifications, changes or deletions; and
- Collect rents, deposits, installment payments arising from the leases and other sums due under leases and agreements with respect to the [REDACTED] Project and give receipts therefor. [REDACTED] shall comply with all applicable State or local laws concerning the responsibility for security deposits and interest; and
- Through the manager of the [REDACTED] Project, hire, discharge and supervise all labor, professionals, agents and employees required for the management, marketing, repair, operation and maintenance of the [REDACTED] Project, except as otherwise provided for herein; and
- Perform obligations of [REDACTED] through attorneys, accountants, agents, independent contractors and employees hired and paid for by [REDACTED] provided that such attorneys, accountants, agents, independent contractors, and employees are licensed, where applicable, under laws of the State of

Ohio to perform the duties for which such parties were hired; and

- On behalf of the City, make contracts for electricity, gas, fuel, water, telephone, sweeping, cleaning and other utility, housekeeping and maintenance services; and
- On behalf of the City, pay all real estate and personal property taxes, insurance premiums, licenses, fees, and payroll taxes incurred in connection with the [REDACTED] Project.

The [REDACTED] Project is located in the City of [REDACTED] historic [REDACTED]. It includes an indoor market, outdoor farmers' market, antique mall, and a glass factory outlet store, with three restaurants, and surrounding parking spaces. The indoor market is a year-round market of approximately [REDACTED] sq. ft. of space contained in the original historic [REDACTED] and [REDACTED] with a total of four "bay" areas. Adjoining the indoor market is the [REDACTED] has approximately [REDACTED] retail vendors and the [REDACTED] has approximately [REDACTED] individual vendors. The [REDACTED] Project is presently 75% leased to tenants. Its anchor tenants, those established businesses that occupy a large amount of leaseable space, are the [REDACTED] leasing [REDACTED] sq. ft. of space, the [REDACTED] leasing [REDACTED] sq. ft. of space, and the [REDACTED] leasing [REDACTED] sq. ft. of space.

Your primary activities, in implementing your management agreement with the City, are supervising, leasing, managing, marketing, maintaining, operating and developing the [REDACTED] Project. Other activities include providing events, entertainment and family activities on selected weekends in the [REDACTED] Project. Also, you will develop a small business management and training program for merchant tenants that would include business and financial planning, marketing and loan packaging. You will also develop a revolving loan fund to provide low-cost financing for business locating in the [REDACTED] Project.

You state that the City of [REDACTED] provides over 50% of your operating budget and the balance of your revenues is derived from tenant rents. Funds will be used for payment of salaries, advertising, maintenance and other operating expenses.

Section 501(c)(3) of the Code provides exemption for organizations that are organized and operated exclusively for educational, charitable, or other exempt purposes.

Section 1.501 (c)(3)-1 (a)(1) of the Income Tax Regulations states that in order for an organization to be exempt as an organization described in section 501 (c)(3), it must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501 (c)(3)-1(b)(1)(i) of the regulations provides that, in general, an organization is organized exclusively for one or more exempt purposes only if its articles of organization limit the purposes of such organization to one or more exempt purposes, and do not expressly empower the organization to engage, otherwise than as an insubstantial part of

its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish such purposes. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(2) of the regulations provides the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense and includes relieving the poor and distressed or the underprivileged, combating community deterioration, lessening neighborhood tensions, and eliminating prejudice and discrimination.

Rev. Rul. 72-369, 1972-2 C.B. 245, provides that an organization formed to provide management and consulting services to unrelated exempt organizations does not qualify for exemption under section 501(c)(3). This Rev. Rul. also states that providing managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit.

Rev. Rul. 74-587, 1974-2 C.B. 162, holds that a nonprofit organization formed to relieve poverty, eliminate prejudice, reduce neighborhood tensions, and combat community deterioration through a program of financial assistance designed to improve economic conditions and opportunities in high density urban areas inhabited primarily by low-income minority or other disadvantaged groups qualifies for exemption under section 501(c)(3) of the Code. The financial assistance provided was in the form of low-cost or long-term loans to, or the purchase of temporary equity interests in, business enterprises otherwise unable to obtain funds from conventional commercial sources due to their location in depressed urban communities or the proprietor's membership in a minority or other disadvantaged group.

Rev. Rul. 76-419, 1976-2 C.B. 146, describes an organization that purchases blighted land in an economically depressed area and converted it into an industrial park. Lots in the park are leased to industrial enterprises on terms sufficiently favorable to attract tenants to the area. Tenants are required by their leases with the organization to hire a significant number of presently unemployed persons in the area and to train them in needed skills. In order to achieve the greatest community benefit, the organization, in selecting tenants for the industrial park, considered only those industrial enterprises whose hiring policies conform to current fair employment legislation. The ruling found that the organization is devoting its resources to uses that benefit the community in ways the law regards as charitable. The organization's activities serve not only to relieve poverty, but also to lessen neighborhood tensions caused by the lack of jobs and job opportunities in the area. Further, by creating an industrial park out of a blighted area, the organization is combating community deterioration. Accordingly, the organization was operated exclusively for charitable purposes and qualified for exemption under section 501(c)(3) of the Code.

Rev. Rul. 77-111, 1977-1 C.B. 144, in Situation 1, held that an organization formed to increase business patronage in a deteriorated area by providing information on the area's

shopping opportunities, local transportation, and accommodations is not operated exclusively for charitable purposes and does not qualify for exemption under section 501(c)(3) of the Code. The overall thrust is to promote business rather than to accomplish section 501(c)(3) objectives exclusively.

In Better Business Bureau of Washington, D.C. v. United States, 316 U.S. 279 (1945), the Supreme Court interpreted the requirement in section 501(c)(3) that an organization be "operated exclusively" by indicating that in order to fall within the claimed exemption, an organization must be devoted to exempt purposes exclusively. This plainly means that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number and importance of truly exempt purposes. The Court held that a better business bureau was not exclusively educational or charitable because its activities were in part aimed at promoting the prosperity and standing of the business community even though there was also benefit to the public.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. No. 31 (1978), the Tax Court held that an organization offering consulting and research services for a fee to various nonprofit organizations did not qualify for exemption under section 501 (c)(3) of the Code. The fees charged were set at or close to cost, but in no event would they be less than the amount needed to cover the cost of providing services. Several factors were listed by the court as militating against exemption. The organization's financing did not resemble that of the typical 501(c)(3) organization in that it did not solicit or receive voluntary contributions from the public. Its only source of income was fees for services. Other negative factors were the manner in which the organization's activities were conducted, the commercial hue of those activities, competition with commercial firms providing similar services and the existence and amount of annual or accumulated profits.

You are not organized and operated exclusively for educational or charitable purposes within the meaning of section 501 (c)(3)-1(c)(2) of the regulations. You are organized and operated to manage the day to day operations of the Erie Street Market. These management activities include leasing space to vendors, providing maintenance services and utilities for the market facility, collecting rent, and providing advertising and promotional marketing for the market facility. Under the circumstances your management and operation of the Erie Street Market constitutes the conduct of a substantial nonexempt activity. Better Business Bureau v. U.S., supra.

Your activities are similar to the management and marketing activities conducted by the organization described in Rev. Rul. 77-111, supra. Like the organization described in Rev. Rul. 77-111 by conducting advertising and marketing as well as managing the market facility you are engaged in activities which promote business in the market place generally rather than accomplish exclusively charitable purposes described in section 501 (c)(3) of the Code.

Your advertising, marketing, and management of the day to day operations of the Erie Street Market are much the same as the management and consulting services provided by the organization described in Rev. Rul. 72-369, supra. The provision of these management services under the circumstances constitutes the conduct of a regular commercial business and a substantial nonexempt purpose. B.S.W. Group, Inc. v. Commissioner, supra.

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Your activities are distinguishable from the activities conducted by the organizations described in Rev. Rul. 76-419 and Rev. Rul. 74-587. The operations of those organizations were conducted in an economically depressed area or directed primarily to low-income minority or other disadvantaged groups and were found to benefit the community in ways the law regards as charitable, such as relieving poverty, eliminating prejudice, reducing neighborhood tensions and combating community deterioration. In contrast, your operation is not located in an economically depressed area nor is it directed primarily to any charitable groups.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you would submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
1111 Constitution Ave, NW
Washington, D.C. 20224
Attn: [REDACTED], T:EO:RA:T:3

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If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

(signed) Robert C Harper, Jr.

Robert C. Harper, Jr.
Manager, Exempt Organizations
Technical Group 3

Form 1937-A	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
CODE	T:EO:RA:T:3	T:EO:RA:T:3				
Surname						
Date						